BLUE RIDGE POWER AGENCY
PROVIDING ELECTRIC ENERGY TO THE BLUE RIDGE

Town of Bedford • City of Danville • City of Martinsville • City of Radford • Town of Richlands • City of Salem
Virginia Polytechnic Institute and State University • Central Virginia Electric Cooperative

April 9, 2018

Karen Sabasteanski
Policy Analyst
Office of Regulatory Affairs
Department of Environmental Quality
PO Box 1105
Richmond, VA 23218

Sent via Email: karen.sabasteanski@deq.virginia.gov
ghg@deq.virginia.gov

Re: Proposed Regulation 9VAC5-140 (Regulation for Emissions Trading Programs)

Dear Ms. Sabasteanski:

The Blue Ridge Power Agency, on behalf of certain members, namely, the Towns of Bedford and Richlands, the Cities of Danville, Martinsville, Radford, and Salem, and the Central Virginia Electric Cooperative, submits comments on regulations proposed by the State Air Pollution Control Board to establish a CO2 Budget Trading Program.

Please contact me if you have any questions about our comments.

Sincerely,

Alice J. Wolfe

Alice Wolfe
General Manager

P. O. Box 2310 • 730 W. Main St. • Salem, VA 24153
Phone: 540/378-0193 • E-mail: brpa@gamewood.net • www.brpa.org

COMMENTS BY THE BLUE RIDGE POWER AGENCY ON PROPOSED REGULATIONS FOR EMISSIONS TRADING PROGRAMS (PROPOSED 9VAC5-140-6010 THROUGH 9VAC5-140-6430)

Blue Ridge Power Agency ("Blue Ridge"), on behalf of certain of its members, namely the Towns of Bedford and Richlands, the Cities of Danville, Martinsville, Radford, and Salem, and the Central Virginia Electric Cooperative ("Commenting Members"), submit the following comments on regulations proposed by the State Air Pollution Control Board ("Board") that would establish a Virginia CO_2 Budget Trading Program ("Program").[1]

I. About Blue Ridge and Commenting Members.

Blue Ridge is a non-profit corporation established in 1988 under the laws of the Commonwealth of Virginia. Blue Ridge is owned and governed by its membership, and has as its mission to further the members' goals of providing reliable power supplies to the residential customers and businesses that they serve—at the lowest rate possible. The Blue Ridge members are "load-serving entities" ("LSEs") that own and operate their own electric distribution systems. They have the same obligation as investor-owned utilities ("IOUs") like Dominion Power to provide reliable electric service to customers, but, unlike an IOU, they operate on a not-for-profit basis. Collectively, the Blue Ridge members serve over 270,000 retail customers in the central and southwestern regions of the Commonwealth.

Blue Ridge members meet their customers' power supply needs by managing balanced portfolios that include generation resource-diverse fuels and technologies, as well as long- and short-term wholesale power contracts with a variety of fuel-diverse resources. Zero carbon-energy is an important component of the Blue Ridge members' overall power supply.

The Blue Ridge Members purchase electric power from zero carbon-emitting resources such as solar, wind, and hydroelectric generation, and from renewable resources like landfill gas-fueled facilities. For instance, Central Virginia Electric Cooperative, Bedford, and Danville are currently purchasing electric energy under long-term agreements from recently-completed solar installations. The group takes power from 13 hydroelectric facilities, including eight that are sited within the Commonwealth. The Cities of Bedford, Danville, Martinsville, and Radford each own small hydroelectric facilities. The City of Martinsville operates a landfill gas generator. The City of Danville offers an energy efficiency program to its customers. Central Virginia Electric Cooperative recently announced a new community solar option that it is making available to its members.

The Commenting Members are concerned that the proposed Program, as currently designed, would raise the cost of power to customers without providing them with equivalent benefits and, more broadly, would fail to achieve the Commonwealth's carbon-reduction goals. The Commenting Members have interests in carbon-free generation but they do not own

[1] *See* 34 Va. Register of Regs. 924 (Jan. 8, 2018) (setting Apr. 9, 2018 comment date) ("Register").

generating facilities that would be subject to the proposed Program; therefore, they will not receive an allocation of consignment allowances that they could sell in the RGGI auctions. The Commenting Members strongly recommend that instead of allocating the consignment allowances to generators, the Board should allocate the consignment allowances to LSEs. This approach would help all LSEs in the Commonwealth to defray the Program's cost impacts in the wholesale power markets. Furthermore, the Commenting Members are concerned that the Board has relied on a study measuring the Program's impact on customer bills that is misleading and unreliable. Blue Ridge offers the following comments on the Program's design flaws and potential remedies.

I. Without Action by the General Assembly, the Board Lacks Statutory Authority Needed to Effectively Implement RGGI.

As a threshold matter, the Commenting Members are concerned that the Board may lack statutory authority to administer the Commonwealth's participation in RGGI and therefore should not act without direction from the General Assembly. Legislatures in the majority of states participating in RGGI have passed authorizing legislation. As a matter of public policy, these state legislatures have determined that because RGGI is a reflection of state policies and will require the citizens to bear a cost to achieve those policies, those elected by the citizens of those states should make the decision as to whether joining RGGI is justified. Virginia, on the other hand, is acting without the benefit of legislative debate and direction. Instead, Governor McAuliffe, by Executive Order, merely directed the Board to implement RGGI. The General Assembly should decide in the first instance whether, and if so how, participation in RGGI is the best way to meet the important goal of reducing carbon emissions in the Commonwealth.

Attorney General Mark Herring, by memorandum issued in November 16, 2017, found that the Board had the statutory authority to implement the Program by regulation. Earlier, in a letter to The Honorable D. Toscano, the Attorney General found that the Board, under existing law, is "authorized to regulate 'air pollution'" and "to promulgate regulations 'abating, controlling and prohibiting air pollution.'"[2] Without any support other than saying that it is "well settled," he determined that greenhouse gases fall within the definition of air pollution under Virginia law.[3] Critics have warned any action to implement RGGI through only administrative action will face a certain court challenge.

To avoid the uncertainty of protracted litigation and to ensure unambiguous support for the Program, the Board should defer action until the General Assembly approves participation in RGGI and authorizes the Department of Environmental Quality ("DEQ") to administer programs that would help to achieve carbon-reduction goals and mitigate the impacts of climate change.

[2] Letter from Mark R. Herring, Att'y Gen., Commonwealth of Va., to The Hon David J. Toscano (May 12, 2017), at 2, 3.

[3] *Id.* at 2.

II. The Program, as Currently Designed, is Flawed.

The proposed Program would establish an initial statewide carbon base budget of either 33 or 34 million tons, which represents the amount of carbon dioxide (CO_2) forecasted to be emitted by the covered units in the Commonwealth in 2020. The rule would not require generators to purchase emissions allowances from the Commonwealth in an auction, thus avoiding a state requirement that all revenue-raising measures must be approved by the General Assembly. Instead, generators would be freely allocated allowances, which they will thereafter consign to the RGGI auction.

Allowances purchased at the RGGI auction would no longer be conditional—meaning that generators would be able to surrender these RGGI allowances to DEQ in order to cover their actual annual CO2 emissions. For each conditional allowance consigned to the auction, the generator would receive the clearing price of the auction. This process allows generators to consign all of their conditional allowances but only purchase what they actually need. Unneeded emissions allowances would be sold, with the proceeds collected by the generator.[4] The Program does not address the treatment of these windfall proceeds and, of notable importance, contains no provision specifying how such windfalls would be returned to consumers.

A. There Is No Reliable Analysis of the Program's Cost Impacts on Customer Bills, and Program Costs Are Likely To Be Much Higher than Proposed.

The impact of the Program on average monthly customers' bills is not reliable, and in fact, the impacts are likely to be considerably higher. The proposed regulations' preamble suggests that the average monthly bill impact for residential, commercial, and industrial consumers through the year 2031 will be nominal—never more than 1.1%.[5] These estimates are taken from an impact analysis prepared by a consultant that "*for purposes of illustration*" adopts the assumption that "95% of revenues that accrue to utilities from the sale of carbon allowances or credits are returned to ratepayers."[6]

No factual basis exists upon which to base an assumption that 95% of the revenues accrued would be returned to customers, particularly customers of the Commenting Members. First, as the DEQ recognizes, the "revenue received by CO_2 Budget Sources owned by regulated electric utilities flow to rate payers pursuant to State Corporation Commission (SCC) requirements."[7] However, there is no legislative or other mandate to require the SCC to impose such a requirement on regulated utilities.[8] At best, the outcome of any proceeding at the SCC

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[4] As described below, the allocation of conditional allowances to covered units is based on historical production, which is an unreliable indicator of future production in the ever changing regional power market administered by PJM Interconnection, L.L.C. ("PJM").

[5] *See* Register at 928 (table 2).

[6] The Analysis Group, Presentation of Virginia IPM Scenario Customer Bill Analysis (Nov. 9, 2017) ("Analysis Group Presentation") at 7 (emphasis in original), *available at* http://www.deq.virginia.gov/Portals/0/DEQ/Air/GHG/bill_analysis.pdf?ver=2017-11-20-145638-017..

[7] Register at 928 (quoting DEQ Nov. 16, 2017 presentation before the Board, p. 24).

[8] *Id.* ("While not described in the regulation, this action is predicated upon anticipated actions of the SCC which it may or may not take"); Va. Dep't of Planning and Budget, Economic Impact Analysis (Dec. 13, 2017) at 7

contemplating a proposal to direct the regulated utilities to return RGGI windfalls to customers is uncertain. Relying on the presumed outcome of an action that may or may not be taken by a different regulatory agency as the basis for cost estimates in this rulemaking process is speculative.

Second, the cost estimates developed by The Analysis Group and relied upon by the Board fail to take into account that a significant share of the covered generators are not subject to the jurisdiction of the SCC. Based on publicly available reports and information provided by the DEQ, approximately one-third of the energy produced in Virginia in 2015 was generated by facilities owned by independent power producers ("IPPs").[9] Those facilities are not regulated by the SCC and, thus, would not be subject to any regulations that may be adopted later by the SCC. These facilities sell power into the regulated wholesale markets and, as a result, those sales are subject to the exclusive jurisdiction of the Federal Energy Regulatory Commission ("FERC").[10] The consultant's study assumes *for illustrative purposes* that "revenues from allowances to independent power producers [would be treated] in the same way as those allocated to utilities (i.e., revenues returned to ratepayers);" however, no state jurisdictional mechanism currently exists to assure that the benefits of allocations to IPPs actually accrue to ratepayers.[11] Thus, the Program as proposed would allow these facilities to make windfall profits off of their allocated share of RGGI allowances, and permit those windfall profits to lay beyond the jurisdictional reach of the Commonwealth's rate regulator. Surely, this approach is contrary to the Program's intent.

The Board should explain why the customer bill impacts should not be adjusted to remove revenues from allowances to unregulated entities, or in the alternative, the Board should explain what state and federal regulatory mechanisms would assure those revenues are returned to customers.

B. All, or a Portion of, the Conditional Allowances Should be Allocated Directly to Load-Serving Entities.

The RGGI model rule leaves it up to states how to allocate allowances. Under Virginia's proposed Program, allowances will be allocated to units based on "the average of the three amounts of the unit's total net-electric output during the three most recent years for which data are available prior to the start of the control period."[12] Thus, all covered units in Virginia, regardless of whether they are regulated by the SCC, will receive an allocation of allowances based on past operation and the right to potentially convert those allowances into windfall

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("This assumed action was incorporated in estimates DEQ provided the Board . . . ."), at 9 ("Assuming that all revenues raised from the auction by regulated utilities are returned to ratepayers, then these producers will not profit, because they cannot keep their sales revenue").

[9] *See* Register at 930.

[10] *See Hughes v. Talen Energy Marketing, LLC*, 136 S. Ct. 1288 (2016).

[11] *See* Analysis Group Presentation at 7 ("For the purpose of this analysis we treat revenues from allowances to independent power producers in the same way as those allocated to utilities (i.e., revenues returned to ratepayers); however, the benefits from allocations to IPPs may not accrue to ratepayers"), *available at* http://www.deq.virginia.gov/Portals/0/DEQ/Air/GHG/bill_analysis.pdf?ver=2017-11-20-145638-017.

[12] Register at 947 (9VAC5-140-6215(A)(2)).

profits. It is noteworthy that no other state has chosen to allocate 95% of allowances to generators.

As proposed, the planned allocation of conditional allowances to generators based on historical usage is arbitrary, and is likely to overcompensate generators and produce excess allowances because energy production at many of the covered units has and will continue to decline as zero-carbon resources (like our members' facilities, described above) compete with high-carbon emitters like coal generation. These excess revenues will be sold at auction or banked by the generators,[13] but those entities that have made investments in energy efficiency and carbon-reducing technologies to achieve the Commonwealth's goals are provided nothing. Further, as discussed above, the Board has stated that the SCC will need to act to require that regulated utilities return auction revenues to customers. But until those rules are finalized there is no guarantee whether or how that will be done and there is a risk that the funds will become windfall profits to the recipients of allowances. It is also manifestly unclear as to how Virginia customers will receive any benefit from the windfall profits earned by unregulated IPPs.

An alternative to the allocation of allowances to units—and we believe this approach to be the prudent course—is directly allocate allowances to LSEs in proportion to their customers' energy consumption.[14] The value could be passed on to those customers by way of offsetting reduction to their bills, or the benefits of programs to invest in local alternative energy projects in their service territories. This approach would not foreclose the statewide set-asides of allowances to support energy efficiency programs. The Commenting Members therefore strongly urge the Board to withdraw the regulations for the purpose of considering whether allocation of consignment allowances should be redirected from generating units to LSEs.

III. The Board Must Take into Account the Program's Secondary Impacts on Wholesale Power Costs.

The preamble to the proposed regulations does not explain how the Program would impact the cost of wholesale power sold to Virginia entities, which it would assuredly do for Blue Ridge's Commenting Members in several ways. These impacts take effect at the wholesale markets regulated by FERC, and the effect could be material. These impacts are discussed below.

First, with respect to Commenting Members' power purchase contracts that include a formulaic type of cost-of-service rates, the cost incurred by the owners of covered generators of procuring RGGI allowances are likely to be passed through in those cost-based rates. However, it is not at all clear whether revenues from the auction for consigned allowances would be credited through the formula rate process and returned to Blue Ridge members. This is a

[13] In most cases, excess allowances will be sold. Banking of excess allowances assumes a need for additional allowances in the future. Generation of power at the covered units is likely to decline over time and, therefore, additional allowances will not be needed.

[14] In California, by contrast, SO_2 allowances are directed to local distribution companies. IOUs in California are required to consign their allowances to auction. Other entities can voluntarily consign their allowances to auction. The revenue from the auction is returned in proportion to the original holders of allowances and the utilities are directed to use that value "for the benefit of ratepayers."

question to be decided by FERC, and could leave members and their consumers with the obligation to bear the costs of RGGI without any offsetting revenues.

Second, energy prices could increase as the cost of RGGI allowances are incorporated into the energy offers that are submitted into the day-ahead and real-time energy markets administered by regional grid operator PJM. Energy prices in the regional markets are determined by the offer of last-dispatched and highest-price resource, and because the auction is a single-price auction the generator's cost of RGGI allowances could have region-wide price impacts.[15]

Over time, the proposed Program would ratchet up the RGGI allowance price and ratchet down available quantity, so the cost of RGGI will become more apparent in wholesale market prices. It follows that Blue Ridge members and others will see a more significant impact of RGGI on their wholesale power costs.

Third, participation in RGGI has the potential to affect congestion paid by the Blue Ridge members. Wherever power is generated, whether in Virginia or even in a different state, it must be moved financially from that location into the Blue Ridge. Regardless of the contract price, if the market price of power at the point of generation, say, in another state, is low (~$30/MWh), and the market price of power in the Blue Ridge area is high (~$35/MWh), the purchaser must pay for the difference between the two prices. Those costs can be substantial.

If the Board decides to proceed with this rulemaking, Blue Ridge's Commenting Members ask the Board to reconsider the allocation of conditional allowances to generators in the first instance. The Regulatory Advisory Panel that worked on the rule last summer was clear: the cost to customers should be a primary consideration in designing any CO_2 trading program. In fact, that panel could not come to consensus on whether load-serving entities or generators should receive the auction credits. Assigning allowances to LSEs is the most direct way to assure that the benefits of RGGI accrue to intended beneficiaries—retail consumers in the Commonwealth. We ask that Governor Northam and the Board withdraw and reconsider the proposed design to ensure that all LSEs are able to keep the cost to end-use customers as low as possible while realizing the benefits that RGGI provides in other states.

[15] For more information about price formation in single-price auctions, *see* "Single Price Auction" at https://en.wikipedia.org/wiki/Single-price_auction.